

**General Information Letter:** Response to request to file composite return (not allowed for tiers of entities).

January 5, 1998

Dear:

This is in response to your letter dated December 18, 1997 in which you request a General Information Letter. Department of Revenue ("Department") regulations require that the Department issue only two types of letter rulings, Private Letter Rulings ("PLRs") and General Information Letters ("GILs"). PLRs are issued by the Department in response to specific taxpayer inquiries concerning the application of a tax statute or rule to a particular fact situation. A PLR is binding on the Department, but only as to the taxpayer who is the subject of the request for ruling and only to the extent the facts recited in the PLR are correct and complete. GILs do not constitute statements of agency policy that apply, interpret or prescribe the tax laws and are not binding on the Department. For your general information we have enclosed a copy of 2 Ill. Adm. Code Part 1200 regarding rulings and other information issued by the Department.

Although you have not specifically requested either type of ruling, the information you have provided requires that we respond with a general information letter. However, given the nature of your inquiry we should be able to address your questions in the context of a general information letter.

In your request you stated:

The purpose of this letter is to request the state's permission to file a non-resident composite return in a unique situation that would result in efficiencies and savings to our client and Illinois.

The Operating Company LLC at the bottom of the accompanying organizational chart is one of a series of LLCs that is being formed to operate in the entertainment business. One such LLC has been formed to distribute films to in-state theaters for commercial exhibition. Other wholly owned subsidiary LLCs have been formed for the production of anticipated films. Each such LLC will be filing as a partnership for federal tax purposes and so qualifies to file on that basis with Illinois. Each of these LLCs will be 99% owned by a common parent, which I have designated "A" near the bottom of the chart, with the remaining 1% owned by a corporation [designated "B" at the right hand side of the chart]. We have advised "A" that it will be subject to the income taxing jurisdiction of all of the states, including Illinois, in which any of the Operating Company LLCs do business. "A" seeks your help in finding a simplified and efficient means by which it may submit applicable tax to Illinois on behalf of as many of the LLC members as possible while avoiding multiple return filing requirements to the full extent possible. It appears that the filing of a composite return by "A" would best serve this purpose.

All income will pass from the Operating Company LLCs through "A" to the ultimate owners. All of the owners are non-resident individuals, with the exception of one foreign, i.e. non-U.S., corporation that is a holder of a portion of the "Other 33.3%" interest shown at the far left side of the chart and designated "C". Even though the partnership structure includes several alternative types of entities (LLCs, limited partnerships, S corporations, and trusts), all of the taxable income derived from "A" will ultimately be attributable to non-resident individuals, except for the income to the income to the indicated foreign corporation. For this reason, we propose that "A" be allowed to account for all of the taxable income and applicable tax liability attributable to the non-resident individuals on a composite return to be filed by "A". [Corporation "B" does not receive any income from "A" and so its income is not involved in this proposal.]

You will want to know that Individual Owner #5 (I5 or "D" at the top middle of the chart), whom I have just been authorized to identify as xxxxxx xxxxxxxxxx as other activities in Illinois that require him to file a non-resident return there. We would not anticipate that "D" could participate in the composite return for non-residents. We would therefore request that S-Corp 2 and LP2 not be required to file the respective information returns in Illinois and that the filing by "A" suffice in this regard. As stated above "A" would not make any composite payments on behalf of "D." Instead, "D" would make his own payments to the state.

The S corporations are the general partners of the three limited partnerships [LP1, LP2, and LP3 in the center of the chart]. They are deriving income from A and must report such income to Illinois. They will not, however, have other activities of any kind that could produce any individual income tax for the state in addition to that which "A" would already be submitting. Since the S corporations' income will be derived solely from "A," we also request that "A" be permitted to pay, on behalf of the S corporations, any taxes that they may owe.

We realize that normal technical filing requirements may discourage the permitting of this type of centralized reporting of the pass-through income of ultimate owners. We submit, however, that this organizational structure presents an ideal opportunity for the state to adopt an innovative and constructive approach to an otherwise complicated and difficult tax compliance problem. This innovative approach would be beneficial both to the state and to "A" and its related parties. If the state permits "A" to file as requested, the related parties would be required to prepare, and Illinois would be required to process, approximately 25 fewer returns. The state would still receive the proper amount of tax to which it is entitled. "A" and its related parties are requesting similar treatment in a number of states. Composite return filings as requested in these states including Illinois could result in substantial tax compliance cost savings to "A" along with similar savings and efficiencies to Illinois.

I am both mailing and faxing this letter to you in the hope that it can receive your early attention since your response will affect filings to take place shortly after the first of the year. I look forward to discussing this further with you. I have just been authorized to identify "a" as xxxxxx xxxxxxxxxx'x "xxxxxxxxxx."

### **Department Analysis**

Section 502 of the Illinois Income Tax Act ("IITA") states in part:

(a) In general. A return with respect to the taxes imposed by this Act shall be made by every person for any taxable year:

- (1) For which such person is liable for a tax imposed by this Act, or
- (2) In the case of a resident or in the case of a corporation which is qualified to do business in this State, for which such person is required to make a federal income tax return, regardless of whether such person is liable for a tax imposed by this Act, unless such person has an Illinois base income of \$1,000 or less and is either claimed as a dependent on another person's tax return under the Internal Revenue Code of 1986, or is claimed as a dependent on another person's tax return under this Act.

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(d) Partnerships. Every partnership having any base income allocable to this State in accordance with section 305(c) shall retain information concerning all income, gain, loss and deduction; the names and addresses of all of the partners, or names and addresses of members of a limited liability company, or other persons who would be entitled to share in the base income of the partnership if distributed; the amount of the distributive share of each; and such other pertinent information as the Department may by forms or regulations prescribe. The partnership shall make that information available to the Department when requested by the Department.

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(f) The Department may promulgate regulations to permit nonresident individual Subchapter S corporation shareholders of the same Subchapter S corporation, and non-resident individuals transacting an insurance business in Illinois under a Lloyds plan of operation, and nonresident individual members of the same limited liability company that is treated as a partnership under Section 1501 (a)(16) of this Act, to file composite individual income tax returns reflecting the composite income of such individuals allocable to Illinois and to make composite individual income tax payments. The Department may by regulation also permit such composite returns to include the income tax owed by Illinois residents attributable to their income from partnerships, Subchapter S corporations, insurance businesses organized under a Lloyds plan of operation, or limited liability companies that are treated as partnership under Section 1501 (a)(16) of this Act, in which case such Illinois residents will be permitted to claim credits on their individual returns for their shares of the composite tax payments. This subsection (f) applies to taxable years ending on or after December 31, 1987.

Accordingly, every individual, partnership or corporation must file its own Illinois income tax return. There is no statutory authority for modifying this system to allow composite reporting for partnerships or corporations except for two limited situations. One is for non-S corporations who are members of the same unitary business group as defined by IITA §1501(a)(27)). The second involves resident and non-resident members of the **same** partnership or Subchapter S corporation under §502(f). However, no statutory language allows multi-tiered reporting of the type proposed by your plan.

Tax law is based on statutory authority and the Department is required to apply the law based upon the wording of the statute. Hence, the Department is unable

to accept composite returns from partnerships, corporations and so on except for the limited instances described above.

If you have additional questions please feel free to contact me at the above address.

Sincerely,

Charles E. Matoesian  
Staff Attorney  
Income Tax Division